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EXEMPTIONS AND LIEN AVOIDANCE UNDER THE BANKRUPTCY REFORM ACT OF 1978 AND OHIO LAW

SPECIFIED PROPERTY of a debtor is exempt from the bankruptcy estate. State law has generally specified the property of a bankrupt which may be exempted from the estate. The Bankruptcy Reform Act of 1978 institutes a new federal policy regarding exemptions. The new federal provisions, however, are under attack. Currently in Ohio, the applicability of the federal avoidance power contained in section 522(f) of the Bankruptcy Code¹ is being questioned. This section provides for the avoidance of certain liens encumbering property otherwise exemptable. Legislation in Ohio specifically provides that the exemption provisions do not affect a security interest of personal property or any lien thereby.² The question of whether or not a debtor in Ohio may utilize the federal avoidance power to claim secured property as exempt, when Ohio prohibits exempting such property, is currently being litigated. Further, there is an underlying issue as to whether the avoidance power is unconstitutional as applied to security interests created prior to the enactment of the Bankruptcy Reform Act of 1978. A review of the Bankruptcy Act of 1898, and the exemption provisions of the State of Ohio will facilitate an understanding of the issues involved in the application of the new federal exemption provisions.

Prior to the enactment of the Bankruptcy Reform Act of 1978,³ the amount and types of property which could be exempted by a debtor were a matter of state law.⁴ Section 6 of the Bankruptcy Act of 1898 provided that:

[T]his act shall not affect the allowance to bankrupts of the exemptions which are prescribed by the laws of the United States or by the State laws in force at the time of the filing of the petition in the state wherein they have had their domicile for the six months immediately preceding the filing of the petition. . . .⁵

Exemption provisions available to debtors vary among the several states. Section 522 of the new Bankruptcy Code attempts to provide a more uniform application of exemptions and do away with antiquated state provisions. The latter concern was recognized in a House Report⁶ as follows:

Most [exemption statutes] are outmoded, designed for more rural times, and hopelessly inadequate to serve the needs of and provide

¹ 11 U.S.C. § 522(f) (Supp. III 1979).

² OHIO REV. CODE ANN. § 2329.661 (Page Supp. 1979).

³ 11 U.S.C. § 522 (Supp. III 1979).

⁴ 11 U.S.C. § 24 (repealed 1978).

⁵ *Id.*

⁶ H.R. REP. No. 595, 95th Cong., 1st Sess. 126, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6087.

a fresh start for modern urban debtors. The historical purpose of these exemption laws has been to protect a debtor from his creditors, to provide him with the basic necessities of life so that even if his creditors levy on all of his nonexempt property, the debtor will not be left destitute and a public charge. The purpose has not changed, but neither have the level of exemptions in many states. Thus the purpose has largely been defeated.

The Bankruptcy Reform Act of 1978 provides exemptions better designed to meet the needs of present day debtors.

Section 522(d)⁷ enumerates the exemptions applicable under federal

⁷ 11 U.S.C. § 522(d) (Supp. III 1979). The section provides:

The following property may be exempted under subsection (b)(1) of this section:

(1) The debtor's aggregate interest, not to exceed \$7,500 in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.

(2) The debtor's interest, not to exceed \$1,200 in value, in one motor vehicle.

(3) The debtor's interest, not to exceed \$200 in value in any particular item, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(4) The debtor's aggregate interest, not to exceed \$500 in value, in jewelry held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(5) The debtor's aggregate interest, not to exceed in value \$400 plus any unused amount of the exemption provided under paragraph (1) of this subsection, in any property.

(6) The debtor's aggregate interest, not to exceed \$750 in value, in any implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor.

(7) Any unmaturred life insurance contract owned by the debtor, other than a credit life insurance contract.

(8) The debtor's aggregate interest, not to exceed in value \$4000 less any amount of property of the estate transferred in the manner specified in section 542(d) of this title, in any accrued dividend or interest under, or loan value of, any unmaturred life insurance contract owned by the debtor under which the insured is the debtor or an individual of whom the debtor is a dependent.

(9) Professionally prescribed health aids for the debtor or a dependent of the debtor.

(10) The debtor's right to receive-

(A) a social security benefit, unemployment compensation, or a local public assistance benefit;

(B) a veteran's benefit;

(C) a disability, illness, or unemployment benefit;

(D) alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;

(E) a payment under a stock bonus, pension, profit sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless-

(i) such plan or contract was established by or under the auspices of an outsider that employed the debtor at the time the debtor's rights under such plan or contract arose;

(ii) such payment is on account of age or length of service; and

(iii) such plan or contract does not qualify under section 401(a), 403(a), 408, 409 of the Internal Revenue Code of 1954 (26 U.S.C. 401(a), 403(a), 408, 409).

law. These exemptions, however, are not mandatory. Congress provides the debtor with an election⁸ between the new federal exemptions⁹ or federal nonbankruptcy exemptions¹⁰ and the exemptions provided by the state of the debtor's domicile. Further, Congress granted the states the power to veto the debtor's right of election.¹¹ The House Report states:

[T]here is a Federal interest in seeing that a debtor that goes through bankruptcy comes out with adequate possessions to begin his fresh start. Recognizing, however, the circumstances do vary in different parts of the country, the bill permits the States to set exemption levels appropriate to the locale, and allows debtors to choose between the State exemptions and the Federal exemptions provided in the bill. Thus the bill continues to recognize the States' interest in regulating credit within the States, but enunciates a bankruptcy policy favoring a fresh start.¹²

For a state to exercise its veto power, legislation must affirmatively be passed opting out of section 522(d).¹³ Inaction on the part of a state will not operate to pre-empt the federal exemptions.¹⁴ With regard to the debtor's option section 522(b) of the Bankruptcy Code¹⁵ provides:

-
- (11) The debtor's right to receive, or property that is traceable to-
- (A) an award under a crime victim's reparation law;
 - (B) a payment on account of the wrongful death of an individual of whom the debtor was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;
 - (C) a payment under a life insurance contract that insured the life of an individual of whom the debtor was a dependent on the date of such individual's death, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor;
 - (D) a payment, not to exceed \$7,500 on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; or;
 - (E) a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

⁸ 11 U.S.C. § 522(b) (Supp. III 1979).

⁹ *Id.* § 522(d).

¹⁰ Federal nonbankruptcy exemptions include: Civil service retirement benefits, 5 U.S.C. §§ 729, 2265; Foreign Service Retirement and Disability payments, 22 U.S.C. § 1104; Longshoremen's and Harbor Worker's Compensation Act death and disability benefits, 33 U.S.C. § 916; special pensions paid to winners of the Congressional Medal of Honor, 38 U.S.C. § 3101; social security payments, 42 U.S.C. § 407; war hazard compensation payments for injury or death hazards, 42 U.S.C. § 1717 (1978); federal homestead lands on debts contracted before issuance of the patent, 43 U.S.C. § 175; Railroad Retirement Act annuities and pensions, 45 U.S.C. § 228(L); Veterans benefits, 45 U.S.C. § 352(E); and wages of fishermen, seamen, and apprentices, 46 U.S.C. § 601.

¹¹ 11 U.S.C. § 522(b)(1) (Supp. III 1979).

¹² H.R. REP. No. 595, 95th Cong., 1st Sess. 126, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6087.

¹³ 11 U.S.C. § 522(b)(1) (Supp. III 1979).

¹⁴ 95 CONG. REC. H11095, 11115 (daily ed. 1978).

¹⁵ 11 U.S.C. § 522(b) (Supp. III 1979) (emphasis added).

- (b) [A]n individual debtor may exempt from property of the estate *either*
- (1) property that is specified under subsection (d) of this section, *unless the State law that is applicable to the debtor under paragraph (2)(A) of this subsection specifically does not so authorize; or, in the alternative,*
 - (2) (A) any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180 day period than in any other place;

A debtor domiciled in a state which opts out is excluded from the election under section 522(b) and is limited to the exemptions granted by the state.¹⁶ A growing number of states, including Ohio, have passed legislation specifically pre-empting Federal exemptions.¹⁷ The tendency of the states to exercise their option frustrates the attempt to establish uniform bankruptcy exemptions throughout the country.

Uniformity of exemption provisions between the states is not required by the Constitution. While the Constitution requires that bankruptcy laws be uniform throughout the United States,¹⁸ this has been interpreted to mean a geographical uniformity rather than a personal uniformity.¹⁹ A rule which operates as to all property which can be reached by legal process is uniform throughout the United States within the meaning of the Constitution.²⁰ The Supreme Court, in *Hanover National Bank v. Moyses*,²¹ held that allowing the states to legislate their own exemptions standards, "was not in derogation of the limitations of uniformity." The court stated that "because all contracts were made with reference to the existing laws, no creditor could recover more from his debtor than the unexempted part of his assets."²² The uniformity requirement is met by providing that the estate of the debtor shall be comprised of all assets which can be reached by legal process.

¹⁶ *Epperly v. Woodyard*, 4 B.R. 124, 2 C.B.C. 2d 60 (Bank. Ct. W.D. Va. 1980); *In re Crump*, 5 B.C.D. 1235, 2 B.R. 222 (Bank. Ct. S.D. Fla. 1980); *In re Stephens*, 5 B.C.D. 1376, Nichols, No. 79-00970 (Bank. Ct. W.D. Va., April 11, 1980).

¹⁷ States which have opted out include: South Dakota, Arizona, Wyoming, Tennessee, Indiana, Georgia, Louisiana, Florida, Virginia, Ohio, and Missouri.

¹⁸ U.S. CONST. art. I, § 8.

¹⁹ *Hanover National Bank v. Moyses*, 186 U.S. 181 (1902); *Stellwagen v. Clum*, 245 U.S. 605 (1918); *Thomas v. Woods*, 173 F. 585 (8th Cir. 1909).

²⁰ *In re Deckert*, 7 F.Cas. 334 (C.C.E.D. Va. 1874).

²¹ 186 U.S. 181.

Ohio, one of several states²³ opting out of the federal exemptions passed emergency legislation to prevent the application of the section 522(d) exemptions.²⁴ Section 2329.662 of the Ohio Revised Code provides that:

Pursuant to the "Bankruptcy Reform Act of 1978," 92 Stat. 2549, 11 U.S.C.A. 522(b)(1), this state specifically does not authorize debtors who are domiciled in this state to exempt the property specified in the "Bankruptcy Reform Act of 1978," 92 Stat. 2549, 11 U.S.C.A. 522(d).

"Thus a debtor domiciled in Ohio may only exempt from property of his estate property that is specified under Ohio Revised Code Section 2329.66."²⁵ The Ohio exemptions limit significantly the amount of property exemptable as compared to the federal provision.²⁶

The Bankruptcy Reform Act of 1978 gives the debtor in a bankruptcy proceeding rights which under the 1898 Act were unavailable. Section 522(f) empowers the debtor to avoid the fixing of certain liens on property to the extent that the lien impairs an exemption.²⁷ Under the Bankruptcy Act of 1898 a debtor's right to an exemption was limited by the value of the debtor's equity in the property.²⁸ If the exemptable property of the debtor was fully secured, the debtor would be unable to utilize the exemption provisions. The Bankruptcy Reform Act of 1978, however, in certain cases, allows the debtor to utilize the exemption regardless of the lien. "The lien is avoided only to the extent of the exemption, and the value of the lien that exceeds the amount that is exempted may still be enforced by the creditor."²⁹ Subsection (f) also provides that a debtor cannot waive the right to avoid liens. This prevents a creditor from requiring such a waiver as a condition for the extension of credit.

²³ See note 17 *supra*.

²⁴ 1979 Ohio Laws 5-307, H.B. No. 674.

²⁵ *In re Hill*, 6 B.C.D. 307, 4 B.R. 310, 313, 2 C.B.C. 2d 123 (Bank. Ct. N.D. Ohio 1980); See also *In re Jones*, No. 680-00437 (Bank. Ct. N.D. Ohio, Aug. 6, 1980).

²⁶ See OHIO REV. CODE ANN. § 2329.66 (Page Supp. 1979).

²⁷ 11 U.S.C. § 522(f) provides:

Notwithstanding any waiver of exemptions, the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section, if such lien is -

- (1) A judicial lien; or
- (2) A nonpossessory, non-purchase-money security interest in any -
 - (A) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry that are held primarily for the personal, family or household use of the debtor or a dependent of the debtor;
 - (B) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or
 - (C) professionally prescribed health aids for the debtor or a dependent of the debtor.

²⁸ 11 U.S.C. § 24 (repealed 1978).

Congress allowed the debtor to void judicial liens on property in order "to undo the actions of creditors that bring legal action against the debtor shortly before bankruptcy. Bankruptcy exists to provide relief for an overburdened debtor."³⁰ The avoidance power assures that "if a creditor beats the debtor into court, the debtor is nevertheless entitled to his exemptions."³¹

A debtor is also permitted to void non-possessory, non-purchase money security interests in certain types of personal property. The policy behind avoiding such liens is expressed in the House Report as follows:

Frequently, creditors lending money to a consumer debtor take a security interest in all of the debtor's belongings, and obtain a waiver by the debtor of his exemptions. In most of these cases, the debtor is unaware of the consequences of the forms he signs. The creditor's experience provides him with a substantial advantage. If the debtor encounters financial difficulty, creditors often use threats of repossession of all of the debtor's household goods as a means of obtaining payment. In fact, were the creditor to carry through on his threat and foreclose on the property, he would receive little, for household goods have little resale value. They are far more valuable to the creditor in the debtor's hands, for they provide a credible basis for the threat, because the replacement costs of the goods are generally high. Thus, creditors rarely repossess, and debtors, ignorant of the creditors' true intentions, are coerced into payments they simply cannot afford to make.³²

The avoidance power contained in section 522(f) is said to eliminate "any unfair advantage creditors have."³³ Secured creditors, however, are asserting that the avoidance power goes well beyond eliminating any "unfair advantage" they might enjoy. The secured creditors are contending that the avoidance power is unconstitutional³⁴ as applied to security interests created prior to the enactment of the Bankruptcy Reform Act of 1978. The avoidance of such a lien is said to deprive the creditor of property without due process of law in contravention of the fifth amendment. This contention has met with some success.³⁵ As the Bankruptcy cases dealing with

³⁰ H.R. REP. No. 595, 95th Cong., 1st Sess. 126 *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6087.

³¹ *Id.*

³² *Id.* at 127.

³³ *Id.*

³⁴ *Centran Bank of Akron v. Ambrose*, 2 C.B.C. 2d 267, 4 B.R. 395 (Bank. Ct. N.D. Ohio 1980); *Credithrift of America, Inc.*, 5 B.C.D. 1306, 2 B.R. 603 (Bank. Ct. E.D. Mich. 1980); *Dotson v. Bradford*, 6 B.C.D. 75 (Bank. Ct. D. Nev. 1980); *Boulton v. General Finance Loan Corp. of Iowa*, 6 B.C.D. 233, 4 B.R. 444 (Bank. Ct. S.D. Iowa 1980); *United States Life Credit Corp. v. Steinart*, 6 B.C.D. 623, 4 B.R. 354, 2 C.B.C. 2d 166 (Bank. Ct. W.D. La. 1980).

³⁵ *Lucero v. Security Industrial Bank*, 4 B.R. 659 (Bank. Ct. D. Colo. 1980); *Jackson v. Security Industrial Bank*, 6 B.C.D. 612, 4 B.R. 293, 2 C.B.C. 2d 91 (Bank. Ct. D. Colo. 1980); *off. No. 80-4149* (10th Cir. Mar. 2, 1981); *Hawley v. Avco Financial Services*, 6

this subject are quite recent, the question of constitutionality of the retroactive application of subsection (f) is still unresolved.

The United States Constitution, declares that Congress shall have the power "to establish . . . uniform laws on the subject of Bankruptcies throughout the United States." Further, Congress is vested with the power "to make all laws which shall be necessary and proper for carrying into Execution the foregoing Powers. . . ." ³⁶ "The subject of 'bankruptcies' includes the power to discharge the debtor from his contracts and legal liabilities, as well as to distribute his property." ³⁷ Congressional power to legislate "was necessarily a grant of power the exercise of which would impair the obligation of contracts." ³⁸

A lienholder's interest may be affected by a bankruptcy court. The court has the power to marshal liens as well as to order the sale of property free of encumbrances, transferring the liens to the proceeds of the sale. ³⁹ "Bankruptcy proceedings constantly modify and affect the property rights established by state law." ⁴⁰ The Supreme Court, in *Wright v. Union Central Life Insurance Co.*, ⁴¹ stated:

Property rights do not gain any absolute inviolability in the bankruptcy court because created and protected by state law. Most property rights are so created and protected. But if Congress is acting within its bankruptcy power, it may authorize the bankruptcy court to affect these property rights, provided the limitations of the due process clause are observed.

The issue raised by secured creditors is that the application of subsection (f) to secured loans made and perfected prior to the effective date of the Bankruptcy Reform Act of 1978 constitutes a deprivation of their security interest without due process of law. ⁴² The standard to be used in

B.C.D. 365, 4 B.R. 147, 2 C.B.C. 2d 80 (Bank. Ct. D. Or. 1980); *Hoops v. Freedom Finance*, 6 B.C.D. 273, 3 B.R. 635 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981); *Rodrock v. Security*, 6 B.C.D. 267, 3 B.R. 629 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981).

³⁶ U.S. CONST. art. I, § 8, cl. 18.

³⁷ *Hanover National Bank v. Moyses*, 186 U.S. at 188.

³⁸ *In re Chicago, R.I.&P. Ry. Co.*, 72 F.2d 443, 452 (7th Cir. 1934), *aff'd*, 294 U.S. 648 (1935).

³⁹ *Wright v. Vinton Branch of The Mountain Trust Bank*, 300 U.S. 440 (1937); *see also* *Van Huffel v. Harkelrode*, 284 U.S. 225, 227 (1931).

⁴⁰ *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502, 517 (1938).

⁴¹ *Id.* at 518.

⁴² *Lucero v. Security Industrial Bank*, 4 B.R. 659 (Bank. Ct. D. Colo. 1980); *Jackson v. Security Industrial Bank*, 6 B.C.D. 612, 4 B.R. 293, 2 C.B.C. 2d 91 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981); *Hawley v. Avco Financial Services*, 6 B.C.D. 365, 4 B.R. 147, 2 C.B.C. 2d 80 (Bank. Ct. D. Or. 1980); *Hoops v. Freedom Finance*, 6 B.C.D. 273, 3 B.R. 635 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981); *Rodrock v. Security*, 6 B.C.D. 267, 3 B.R. 629 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981).

determining whether or not bankruptcy legislation has transgressed the limitations of the Due Process Clause is not entirely clear.

In the case of *Hanover National Bank v. Moyses*, the Supreme Court stated the standard to be that "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law. . . ." ⁴³ In *Hanover*, the plaintiff asserted that it had been deprived of property without due process of law because the Bankruptcy Act of 1898 did not require that personal notice of the filing of the petition or of the application for discharge be given to creditors in a voluntary proceeding. ⁴⁴ The Court noted that Congress had the power to legislate on the subject of bankruptcies and that such power extended to impairing the obligation of contracts. ⁴⁵ The act drawn in question in that case was found to be reasonable. The Court reasoned that as bankruptcy proceedings are "in the nature of proceedings in rem. . . [s]ervice of process or personal notice is not essential to the binding force of the decree." ⁴⁶ The exercise of this power by Congress was held to be constitutional since it was "not so grossly unreasonable as to be incompatible with fundamental law." ⁴⁷

The later Supreme Court decision of *Louisville Joint Stock Land Bank v. Radford* examined the constitutionality of an act that provided for appraisal of encumbered farm property and repurchase by the bankrupt at the newly appraised value or rental of the property for five years with an option to repurchase. ⁴⁸ At issue was whether Congress deprived creditors of substantially valuable property rights without compensation. ⁴⁹ The Court described the act as taking "from the mortgagee rights in the specific property held as security; and . . . [scaling] down the indebtedness to the present value of the property." ⁵⁰ The Court determined that under state law the following property rights had been taken from the mortgagee:

- (1) The right to retain the lien until the indebtedness thereby secured is paid.
- (2) The right to realize upon the security by a judicial public sale.
- (3) The right to determine when such sale shall be held, subject only to the discretion of the court.
- (4) The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt. . . .

⁴³ 186 U.S. 181, 192 (1902).

⁴⁴ *Id.* at 181.

⁴⁵ *Id.* at 188.

⁴⁶ *Id.* at 192.

⁴⁷ *Id.*

⁴⁸ 295 U.S. 555 (1935).

⁴⁹ *Id.* at 601.

- (5) The right to control meanwhile the property during the period of default, subject only to the discretion of the court, and to have the rents and profits collected by a receiver for the satisfaction of the debt.⁵¹

The Court noted that "under the bankruptcy power Congress may discharge the debtor's personal obligation. . . . But the effect of the act here complained of is not the discharge of Radford's [the debtor's] personal obligation."⁵² Rather the Court believed that the purpose of the legislation was to preserve the ownership and enjoyment of the farm in the mortgagor.⁵³ The Court held this to be beyond congressional power⁵⁴ and an unconstitutional taking of property.

It is well established⁵⁵ that one of the legitimate purposes of bankruptcy is to provide the debtor with a fresh start. Further, "there is a federal interest in seeing that a debtor that goes through bankruptcy comes out with adequate possessions to begin his fresh start."⁵⁶

The very essence of a national bankrupt system . . . [includes:] the making of such reasonable exemptions of property to the bankrupt as will keep him from absolute poverty, give him some means to commence life anew, support and educate his family, and make him a good and useful citizen.⁵⁷

Subsequently the Supreme Court, in *Wright v. Vinton Branch of The Mountain Trust Bank*,⁵⁸ stated that the constitutionality of bankruptcy legislation depended upon "whether the legislation modifies the secured creditor's rights, remedial or substantive, to such an extent as to deny the due process of law guaranteed by the Fifth Amendment."⁵⁹ The Court went on to conclude that the mortgagee's rights were not unreasonably modified by the legislation which extended the period within which a debtor could redeem the mortgaged property.⁶⁰

The *Radford* case is relied upon by those bankruptcy courts which have found section 522(f) unconstitutional.⁶¹ The bankruptcy court, in

⁵¹ *Id.* at 594-95.

⁵² *Id.* at 589.

⁵³ *Id.* at 594.

⁵⁴ *Id.*

⁵⁵ See *Hanover National Bank v. Moyses*, 186 U.S. 181 (1902).

⁵⁶ H.R. REP. No. 595, 95th Cong., 1st Sess. 126 (1977); reprinted in [1978] U.S. CODE & AD. NEWS 5963, 6087.

⁵⁷ *In re Vogler*, 28 F. Cas. 1248 (D.C.W.D. N.C. 1873).

⁵⁸ *Wright v. Vinton Branch of The Mountain Trust Bank*, 300 U.S. 440 (1937).

⁵⁹ *Id.* at 470.

⁶⁰ *Id.* at 460-61.

⁶¹ See *Jackson v. Security Industrial Bank*, 6 B.C.D. 612, 4 B.R. 293, 2 C.B.C. 2d 91 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981); *Hawley v. Avco Financial Services*, 6 B.C.D. 365, 4 B.R. 147, 2 C.B.C. 2d 80 (Bank. Ct. D. Or. 1980); *Hoops v. Freedom Finance*, 6 B.C.D. 273, 3 B.R. 635 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549

Rodrock v. Security Industrial Bank followed *Radford* stating that it stood for "the proposition that a substantive right in specific property cannot be substantially impaired by legislation enacted after the right has been created without doing violence to the property owner's rights to due process."⁶² The court went on to conclude that this principle was still viable and had not been overruled by subsequent cases.⁶³ The court then stated that "legislation which effects the total deprivation of a substantive right in specific property antedating the statute is unreasonable." The extinguishing of a creditor's nonpossessory, nonpurchase-money security interest was held to be a "total deprivation of a substantive right in specific property."⁶⁴

The Court of Appeals for the tenth circuit in affirming *Rodrock* stated:

[A]lthough Congress, under the bankruptcy power, may discharge a debtor's personal obligation, because, unlike the states, Congress is not prohibited from impairing the obligation of contract, nevertheless Congress could not take for the debtor's benefit, rights in specific property acquired by a creditor prior to the amendment of the Bankruptcy Act.^{64a}

While *Radford* has not been expressly overruled, the principle involved there scaling down the indebtedness owing to a mortgagee to the present appraisal value, held to be unconstitutional in *Radford*, was later held to be constitutional by the Supreme Court in *Wright v. Union Central Life Insurance Co.*⁶⁵ The Court stated that the creditor did not have a constitutional claim beyond the present value of the property.⁶⁶ The Court declared:

[T]he Act must be liberally construed to give the debtor the full measure of the relief afforded by Congress . . . lest its benefits be frittered away by narrow formalistic interpretations which disregard the spirit and the letter of the Act.⁶⁷

The test enunciated in *Radford* should not be expanded to include

(10th Cir. Mar. 2, 1981); *Rodrock v. Security*, 6 B.C.D. 267, 3 B.R. 629 (Bank. Ct. D. Colo. 1980), *aff'd* No. 80-1549 (10th Cir. Mar. 2, 1981).

⁶² 6 B.C.D. 267, 270, 3 B.R. 629, 632.

⁶³ *Id.* See *Wright v. Vinton Branch of The Mountain Trust Bank*, 300 U.S. 440 (1937); *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502 (1938); *Wright v. Union Life Ins. Co.*, 311 U.S. 273 (1940).

⁶⁴ 6 B.C.D. at 270, 3 B.R. at 632.

^{64a} *Rodrock v. Security Industrial Bank*, No. 80-1549, slip op. at 10 (10th Cir. Mar. 2, 1981). The court of appeals held that the intent of Congress was to apply section 522(f) retroactively. The court stated "if the Reform Act were applied only to those cases commenced after October 1, 1979, which involved security interests which came into existence after that date, there would be no bankruptcy law applicable to cases filed after October 1, 1979, but involving security interests which were fixed prior to October 1, 1979." *Id.* at 8. Creditors holding security interests prior to the enactment of the Reform Act were found to possess specific property rights which constitutionally could not be taken for the benefit of debtors. *Id.*

⁶⁵ 311 U.S. 273.

⁶⁶ *Id.* at 278.

⁶⁷ *Id.* at 279, citing *John Hancock Mutual Life Ins. Co. v. Bartels*, 308 U.S. 180 (1939); *Kolb v. Feverson*, 308 U.S. 433 (1940).

circumstances not then present before the Court. The lien in *Radford* attached to specific real property rather than to the general property of a consumer debtor. Further, the property right which was held to be substantial in *Radford*, was later held not to give rise to a constitutional claim in *Wright*.

While there is support for the position taken in *Rodrock*, it is not consonant with the policy of affording the debtor a fresh start. Congress's power to legislate on the subject of bankruptcies encompasses the passing of laws which are necessary and proper to carry out its express power.⁶⁸ The avoidance power provided by Congress is indeed necessary to provide the debtor with a fresh start and to maintain minimal provisions so as to prevent the debtor from becoming a public charge. Lending institutions frequently take blanket liens covering all household goods in exchange for a loan to a consumer debtor. The property covered by such a lien has little intrinsic value to the lender. The actual usefulness of such a lien is the leverage it provides over a debtor both before and during bankruptcy.⁶⁹ Before bankruptcy the lien is used to squeeze payments out of the debtor. During bankruptcy "the secured creditor would threaten to repossess the property subject to its security interest unless the debtor reaffirmed his debt."⁷⁰ Absent the avoiding power, a blanket lien on household goods would preclude a debtor from exercising his or her right to exempt household goods. Section 522(f) is a necessary and appropriate means of carrying out the express power of Congress to establish bankruptcy laws.

It cannot be said that the avoidance of a lien, to the extent that it impairs an exemption, totally deprives a creditor of a substantial right in specific property. First, the avoidance power does not work a total deprivation of a security interest unless the value of the secured property is less than or equal to the amount allowed by the exemption. Section 522(f) expressly provides that a lien is avoided only to the extent it impairs the exemption. The maximum amount by which a lien could be avoided is the full amount of the exemption.⁷¹ "The value of the lien that exceeds the amount that is exempted may still be enforced by the creditor."⁷²

Second, creditors taking a nonpurchase—money security interest in household goods do not necessarily do so because of the value of the goods. In *Rodrock*, the court held that the retroactive application of the avoidance power deprived the secured creditor of a substantial right in specific prop-

⁶⁸ U.S. CONST. art. I, § 8, cl.18.

⁶⁹ *Credithrift of America, Inc. v. Meyers*, 5 B.C.D. 1306, 1307, 2 B.R. 603, 606 (Bank. Ct. E.D. Mich. 1980).

⁷⁰ *Id.*

⁷¹ Under § 522(d)(5) of the federal exemption provisions, the debtor is entitled to any unused portion of the exemption in § 522(d)(1).

⁷² *COLLIER ON BANKRUPTCY* § 522.29 (15th ed. 1979).

erty. The right to secured property rests upon the fact that the security interest was created in order to provide the creditor with an alternative means of repayment in the event the debtor defaults upon the debt.⁷³ The nature of a security interest was described in *In re Carter*, as follows:

The creditor lends money because of his belief that the property is worth at least the amount of the loan and because of his willingness to take the property in lieu of the debt in case the debt is not paid. This is the foundation, the essential element of every such contract.⁷⁴

"This is not the case where a creditor takes a nonpurchase-money security interest in the debtor's household and personal goods."⁷⁵ While holding subsection (f) constitutional, the bankruptcy court for the Northern District of Ohio, in *Centran Bank of Akron v. Ambrose*, stated:

A creditor who makes a loan and takes a nonpurchase-money security interest in highly depreciable household goods as security for the loan, does not actually take the household goods as security for the loan because there is no belief by the creditor that the household goods are worth the amount of the loan. The relationship between the value of the security amount and the amount of the loan that is present in a mortgage of real estate is not present in a nonpurchase-money lien on household goods.⁷⁶

Such a nonpossessory, nonpurchase-money lien is not viewed by the creditor as a substantial right in specific property,⁷⁷ nor should it be so regarded by the courts.

Further, Congress recognized that there is an inherent difference between a lien which attaches to specific property and a blanket lien applying to all property in general. Section 522(f) of the Bankruptcy Code was only made applicable to general liens.⁷⁸ The distinction between a general and a specific lien is also recognized in other contexts. In cases involving the federal priority provisions,⁷⁹ wherein debts owed to the federal government in a non-bankruptcy setting are given priority, the Supreme Court has held that the federal government takes priority over a perfected security interest which is not specific as to the property to which it attached.⁸⁰ The

⁷³ *Centran Bank of Akron v. Ambrose*, 4 B.R. 395, 399, 2 C.B.C. 2d 267 (Bank. Ct. N.D. Ohio 1980).

⁷⁴ *In re Carter*, 56 F. Supp. 385, 393 (W.D. Va., 1944).

⁷⁵ *Centran Bank of Akron v. Ambrose*, 4 B.R. 395, 399, 2 C.B.C. 2d 267, 271 (Bank. Ct. N.D. Ohio 1980).

⁷⁶ *Id.* at 400, 2 C.B.C. 2d at 272.

⁷⁷ H.R. REP. No. 595, 95th Cong., 1st Sess. 127 (1977) reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6088.

⁷⁸ Section 522(f) is only applicable to judicial liens and nonpossessory, nonpurchase-money security interests in certain property.

⁷⁹ 31 U.S.C.A. § 191 (1980 Supp.).

⁸⁰ *Gordon v. Campbell*, 329 U.S. 362 (1946). In that case the Court stated that for a perfected security interest to take priority over the federal government the lien must be

rights of a creditor in the property subject to a nonpossessory, non-purchase-money security interest are not rights in specific property such as to defeat the legitimate exercise of Congress's legislative power.

Congress's legislative power is unrestricted and paramount.⁸¹ Further, the power of Congress to legislate on the subject of bankruptcies is read into contracts.⁸² The Supreme Court, in *Home Building and Loan Association v. Blaisdell*, stated:

Not only are existing laws read into contracts in order to fix obligations, as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order.⁸³

Congress has the power to pass laws which are necessary and proper to establish uniform laws on the subject of bankruptcies. With such authority, Congress "is the sole judge of the means and their appropriateness to the purpose of the legislation so long as said means [do] no violence to the provisions of the constitution."⁸⁴ Whether due process has been denied by the enactment should be judged by whether the law is "so grossly unreasonable as to be incompatible with fundamental law."⁸⁵ This is the standard enunciated in *Hanover* and later used in *Wright v. Vinton Branch of The Mountain Trust Bank*.⁸⁶ As stated in *Ambrose*:

Section 522(f) of the Bankruptcy Code is addressed to the legitimate end of protecting the debtor's exemptions, his discharge, and thus his fresh start and the means taken, permitting the debtor to avoid certain liens on certain exempt property, are reasonable and appropriate to that end.⁸⁷

While the constitutionality of section 522(f) has yet to be determined by an appellate court,⁸⁸ it is not an unreasonable modification of the creditor's rights. Further, the avoidance power enjoys a presumption of constitutionality with the complaining party bearing the burden of establishing a due process violation.⁸⁹

definite as to the identity of the lienor, the amount of the lien, and the property to which it attaches. See also *United States v. Gilbert Associates, Inc.*, 345 U.S. 361 (1953), where the Court required title or possession of the property to pass to the lienor.

⁸¹ *International Shoe Co. v. Pinkus*, 278 U.S. 261, 265 (1929).

⁸² *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502, 516 (1938).

⁸³ *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 435 (1934).

⁸⁴ *In re Chicago, R.I.&P. Ry. Co.*, 72 F.2d 443, 450 (7th Cir. 1934).

⁸⁵ *Hanover National Bank v. Moyses*, 186 U.S. 181, 193 (1902).

⁸⁶ 300 U.S. 440.

⁸⁷ 4 B.R. at 401.

⁸⁸ To date there are no appellate court decisions deciding the constitutionality of section 522(f).

⁸⁹ *Ferguson v. Skrupa*, 372 U.S. 726 (1963); *Williamson v. Lee Optical Co.*, 348 U.S. 483 (1955); *Metropolitan Cas. Ins. Co. v. Brownell*, 294 U.S. 580 (1935).

The question of whether or not the federal avoidance power may be invoked by a debtor in Ohio to retain secured property otherwise exemptable is presently being disputed. The State of Ohio has affirmatively opted out⁹⁰ of the federal exemptions⁹¹ and further has expressly legislated that the state exemptions do not affect or invalidate a security interest of any personal property, or any lien created thereby.⁹² The problem of whether the state statute prevents the application of the avoidance power arises because of the language in section 522(f) which allows a lien to be avoided "to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b)."⁹³ Section 522(b) allows a debtor to exempt from property of the estate "property that is specified under subsection (d) of [section 522] . . . unless the State law [that is applicable to the debtor] . . . specifically does not so authorize [And a] debtor domiciled in Ohio may only exempt from property of his estate property that is specified under Ohio Revised Code Section 2329.66."⁹⁴ Secured property may not be exempted by a debtor in Ohio. This has been interpreted by one court⁹⁵ to preclude the applicability of subsection (f) in Ohio, as there are no exemptions to protect.

The real issue involved is whether Congress authorized the states to opt out of the avoidance power as they did the exemption provisions. Nowhere does it appear that Congress intended the states to be able to preempt other substantive areas of bankruptcy law.⁹⁶ Subsection 522(b) allows a debtor to exempt property specified in subsection (d) unless the state law specifically does not so authorize. The state is given express authority to prevent the application of the exemptions listed in subsection (d). No such authority is conferred upon the states for preventing the application of subsection (f). Further, the House Report states that "the bill permits the States to set exemption levels."⁹⁷ This indicates a Congressional intent to allow the states to merely alter the amounts of the exemption, not to further alter the substantive rights of the debtor under subsection 522(f). "The logical conclusion which follows is that Congress provided the authority stated in subsection 522(b) to allow states to select exemption listings, and would have specifically included any further authority if intended."⁹⁸ The avoid-

⁹⁰ OHIO REV. CODE ANN. § 2329.662 (Page Supp. 1979).

⁹¹ 11 U.S.C. § 522(d) (Supp. III 1979).

⁹² OHIO REV. CODE ANN. § 2329.661 (Page Supp. 1979).

⁹³ *In re Hill*, 6 B.C.D. 307, 4 B.R. 310, 313, 2 C.B.C. 2d 91, (Bank. Ct. N.D. Ohio (1980)).

⁹⁴ *Id.*

⁹⁵ *Panesky v. CIT Financial Services*, 5 B.R. 201 (Bank. Ct. N.D. Ohio 1980).

⁹⁶ *In re Hill*, 6 B.C.D. 307, 4 B.R. 310, 2 C.B.C. 2d 91 (Bank. Ct. N.D. Ohio 1980); *Cox v. Blazer Financial Services, Inc.*, 6 B.C.D. 434, 4 B.R. 240, 2 C.B.C. 2d 255 (Bank. Ct. S.D. Ohio 1980).

⁹⁷ H.R. REP. NO. 595, 95th Cong., 1st Sess. 126 (1977) reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6087.

⁹⁸ *Cox v. Blazer Financial Services, Inc.*, 6 B.C.D. 434, 4 B.R. 240, 2 C.B.C. 2d 255.

ance power was made applicable to all states irrespective of whether they affirmatively opted out of the federal exemptions.

As section 522(f) is an independent power, it is beyond the power of the State of Ohio to enact or enforce a law which conflicts with the federal bankruptcy provision.⁹⁹ Federal bankruptcy legislation governs where there is a conflict with state law because it is the "supreme Law of the Land."¹⁰⁰ It follows that Ohio Revised Code Section 2329.661(c) is inoperative where it conflicts with the federal avoidance power in section 522(f) of the Bankruptcy Code.

Thus, a debtor domiciled in Ohio may utilize section 522(f) to avoid a lien to the extent that it impairs an exemption to which a debtor is entitled. State law controls the amount of the exemption available to the debtor in Ohio. The State of Ohio revised its exemption statute¹⁰¹ when it opted out of the federal provisions. The new exemption levels provided by the state, however, cannot be applied to debts incurred before the effective date of the statute.¹⁰² To retroactively apply state exemptions would impair the obligation of the contract "and this the states were forbidden to do."¹⁰³ The Supreme Court, in *Edwards v. Kearzey*, stated:

The remedy subsisting in a state when and where a contract is made and is to be performed is a part of its obligation, and any subsequent law of the state which so affects that remedy as substantially to impair and lessen the value of the contract is forbidden by the Constitution, and is, therefore, void.¹⁰⁴

The state exemption statute as revised would alter the obligation owing to a creditor on a pre-existing contract. Further, Congress cannot empower the states, via section 522(b), to alter such an obligation.¹⁰⁵ Since the states are forbidden to impair the obligation of a contract by the Constitution,¹⁰⁶ the exemption statute cannot be applied to a debt incurred prior to the effective date of the statute.

A debtor domiciled in the State of Ohio is empowered to avoid certain liens to the extent that they impair an exemption to which they are entitled under state law. Section 522(f) grants this power even though

⁹⁹ *International Shoe Co. v. Pinkus*, 278 U.S. 261, 265 (1929); *Perez v. Campbell*, 402 U.S. 637, 652 (1971).

¹⁰⁰ U.S. CONST. art. VI, cl.2.

¹⁰¹ OHIO REV. CODE ANN. § 2329.66 (Page Supp. 1979).

¹⁰² *In re Fox*, 16 F. Supp. 320 (S.D. Cal. 1936); *Bank of Minden v. Clement*, 256 U.S. 126 (1921); *Gunn v. Barry*, 82 U.S. (15 Wall.) 610 (1872); *Edwards v. Kearzey*, 96 U.S. 595 (1877).

¹⁰³ *Hanover National Bank v. Moyses*, 186 U.S. 181, 188 (1902).

¹⁰⁴ 96 U.S. 595, 607.

¹⁰⁵ *Gunn v. Barry*, 82 U.S. (15 Wall.) 610 (1872); *Kener v. La Grange Mills*, 231 U.S. 215 (1913).

the state has affirmatively opted out of the federal exemptions. Thus, the debtors exemptions and fresh start are protected throughout the United States. This result reflects the congressional awareness of the unique problems facing the consumer debtor in our credit-oriented society.

KAREN L. EDWARDS

COMPARATIVE NEGLIGENCE IN OHIO: PROSPECTIVE OR RETROSPECTIVE APPLICATION

INTRODUCTION

JUNE 20, 1980, the effective date of Ohio Revised Code § 2315.19,¹ is a watershed in Ohio tort law. It hails a long awaited new era in which the negligent defendant can no longer exculpate himself entirely because of the slightest fortuitous fault of the plaintiff. But will the ameliorative impact of this statute be felt immediately? Will the plaintiff whose injury precedes this date be touched by its equitable results? The answer to this question is vital in the transition represented by the statute of limitations for tort actions. It is an issue which the lower courts are now confronting and which is unlikely to be resolved until the Ohio Supreme Court settles the matter.

Section 2315.19 replaces the common law doctrine of contributory negligence with a more equitable version of this historic, but anachronistic tort defense. With its enactment, Ohio joined an increasing majority of jurisdictions. By 1977 there was no longer any doubt; comparative negligence, in one form or another, had replaced contributory negligence in at least thirty-two states and Puerto Rico.² It is now the prevailing doctrine in the United States.

Under Revised Code § 2315.19, the contributory negligence of the plaintiff is no longer an absolute bar to recovery. Only where a plaintiff's fault is greater than that of all defendants combined is that plaintiff precluded entirely from recovery.³ Thus under the new Ohio statute, the possibility of recovery for the negligent plaintiff is significantly enhanced while at the same time liability exposure of the defendant is proportionately enlarged. It is therefore of critical importance to determine whether such an alteration in the relative rights of litigants is constitutional.

¹ OHIO REV. CODE ANN. § 2315.19 (Page Supp. 1980).

² V. SCHWARTZ, *COMPARATIVE NEGLIGENCE* 1 (Supp. 1978).

³ OHIO REV. CODE ANN. § 2315.19(A)(1) (Page Supp. 1980).